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The WTO Agreement on Basic Telecommunications: a reevaluation

Chantal Blouin*

University of Toronto and Department of Foreign Affairs and International Trade, 125 Sussex Drive, Ottawa, ON, Canada K1A 0G2

Abstract

This paper discusses the benefits and the weaknesses of the World Trade Organization (WTO) Agreement on Basic Telecommunications. The Agreement is aimed at opening national telecommunications services markets to foreign competitors as well as setting rules to ensure fair competition. Previous assessment of the Agreement raised three main shortcomings: the limited scope of liberalization created by the Agreement, the lack of precision of the regulatory principles of the Reference Paper and the weaknesses of the sectoral approach in comparison with a more horizontal approach to competition policy and domestic regulation. This paper challenges these views and emphasizes the importance of the Agreement and the Reference Paper on regulatory principles in particular.

Keywords: World Trade Organization (WTO); Basic telecommunications

1. Introduction

The inclusion of services in the multilateral trade regime was recognized as an important achievement of the Uruguay Round. Up to recently, services were not even seen as being tradable. Through the gradual evolution of how services are envisioned, it became internationally accepted to include them into the regime for international trade. The General Agreement for Trade in Services (GATS) in 1994 was the result of this new understanding. However, the commitments taken by the World Trade Organisation (WTO) members in the Uruguay Round regarding services were limited to specific sectors. One central sector where very few commitments were taken by the end of the Uruguay Round was basic telecommunications services.

* Tel.: +1-202-225-2331; fax: +1-202-226-0836.
E-mail address: chantalblouin@msn.com (C. Blouin)

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Telecommunication services markets presented some unique features which made them less prone to competition than other services sectors. First, the domestic markets were, in most cases, completely dominated by a national monopoly. This single provider was often owned by the State, which created worries about the independence of the domestic regulator. The legacy of a monopolistic market structure was also a subject of concern. It was feared that the incumbents (the suppliers who were the monopoly providers prior to liberalization) would have an unfair advantage compared to the new entrants. One of the incumbents' strategic advantage is their control of the existing networks of communications. Most new entrants need to connect to this network to offer their services. By refusing access to this network or by asking unreasonable charges for access, the incumbents can keep potential competitors at bay.

Despite these concerns and given the importance of this sector as an industry and an infrastructure enabling other types of trade, negotiations continued and an agreement was finally reached in 1997 to place telecommunications services under the GATS, according to the specific commitments of each country. The Agreement on Basic Telecommunications (ABT) reached on February 15, 1997 by the members of the World Trade Organization (WTO) sets new rules concerning trade in telecommunications services.[1] This paper discusses the consequences of this new agreement. Previous analysis stressed the shortcomings of the ABT and the Reference Paper on regulatory principles which accompanied it (Bronkers & Larouche, 1997; Fredebeul-Krein & Freytag, 1997). This paper challenges their pessimistic views. A descriptive section precedes the evaluation of the strengths and weaknesses of the ABT.

2. Description of the WTO's Agreement on Basic Telecommunications

Negotiations on telecommunications services officially began under the auspices of the GATT in 1986 during the Uruguay Round, but the first three years were centered on creating an outline of a general agreement on services. In 1994, at the end of the round, no agreement on basic telecommunications was reached, but a General Agreement on Trade in Services (GATS) was concluded.[2] This agreement set the general framework within which discussions on telecommunications would take place. The GATS calls on WTO Members to observe 14 general obligations such as the non-discrimination and regulatory transparency (Hoeckman & Kostecki, 1995). In addition to the general obligations, the GATS takes the form of national schedules of commitments. The schedules are usually organized on a sectoral basis, even though horizontal

[1] International trade in telecommunications services takes two main forms: cross-border supply and commercial presence. Cross-border trade is the most important mode of international transactions in telecommunications services. It consists in international telephone calls, i.e. the placement of a call in a home market which is terminated in a foreign market. In 1995, these services generated 52.8 billion US$ in retail revenues. The second form of telecommunications services trade is through foreign investment to establish commercial presence. Until recently, this form of trade was very restricted because the provision of telecommunications services in most countries was the responsibility of one single organization which was entirely state-owned.

[2] Negotiations were formally concluded at the Ministerial Meeting held in April 1994 in Marrakech, Morocco. The Final Act embodying its results came into force on 1 January 1995. An Annex on Telecommunications was attached to the GATS. This annex aimed at ensuring that suppliers of various services have access to the telecommunications networks of the country where they are conducting business.

commitments are also possible. These commitments can be made on market access or national treatment disciplines with respect to four modes of supply. In the Uruguay Round, several countries took specific market-access and national treatment commitments in the value-added telecommunications services (transmissions which include some data processing), but very few on basic telecommunications. Consequently, a Negotiating Group on Basic Telecommunications (NGBT) was created at the end of the Uruguay Round to continue discussions on this topic with the objective of reaching an agreement in 1996. These negotiations broke down as the United States claimed that a critical mass of market-access commitments was not reached. Members nevertheless agreed to further extend the negotiations and in February 1997, an Agreement on Basic Telecommunications was finally concluded.

This agreement included 55 schedules of specific commitments (accounting for 69 countries, the EU presenting a single schedule) regarding market-access and national treatment of foreign telecommunications services providers. Members could specify which segments of the telecommunications services sector they wish to open to foreign competition (local or long-distance services, international calls, mobile telephony). Except for Turkey, members of the OECD liberalized all segments of the telecommunications services sector.

Moreover, almost all the signatories to the ABT included additional commitments concerning regulatory principles in their schedules. These regulatory principles are included in the Reference Paper, a short document negotiated in 1996. Most Members took binding commitments on these regulatory principles by including the Reference Paper in their schedule of commitments (in the additional commitments section).[3]

The Reference Paper (RP) aimed to address the issue of the dominance of the incumbents and to ensure that competitive conditions are created. Indeed, the lifting of the formal barriers to entry is not sufficient to ensure actual market access, given the strength of the traditional national operators in their domestic market and their control over essential facilities such as the local telecommunications network. In telecommunications services, the historical market structure has been a monopolistic one. Whether owned by the state or by private interests, the national monopoly has been responsible for the provision of all telecommunications services. Even after the introduction of competition, the problem of the dominance of the "incumbent" remains.

Several countries such as Australia, Canada, Japan, New Zealand, Sweden, United Kingdom, United States lifted many of the legal and regulatory barriers for domestic entrants in telecommunications services markets in the 1980s and 1990s (OECD, 1995). These early experiences with competition, even though considered successful in terms of their effect on price and quality, confirmed that given the market power of the incumbents, there was a need for special safeguards in order to create conditions for actual competition.

The goal of the Reference Paper is to create these conditions. The document has five main sections. It first deals with the prevention of *anticompetitive behavior* such as cross-subsidization, the use of information obtained by competitors and the withholding of technical or commercial information. The second element of the RP is *interconnection*. This is the core of the RP because most new entrants cannot build their own complete telecommunications network at once, given the need for prohibitively large capital investments. Hence, they need to lease part of the incumbent's

[3] Bolivia, India, Malaysia, Morocco, Pakistan, the Philippines, Turkey and Venezuela did not include the whole document and Bangladesh, Mauritius and Thailand will adopt it later.

network to be able to provide their services. Moreover, the new entrants' customers have to be connected with incumbents' clients so that everybody on the network can communicate (network externality). The RP specifies that interconnection with the major supplier should be provided:

- at any technically feasible point in the network,
- under nondiscriminatory, transparent and reasonable terms and rates and the quality of the service should be "no less favorable" than the service provided to subsidiaries,
- in timely fashion,
- at cost-oriented rates, and
- and sufficiently unbundled.

The procedures of the negotiations and the interconnection arrangements between the major supplier and the new entrants must be public and transparent. An independent body must resolve disputes, if negotiations are not successful.

The third section of the RP requires that *universal service* obligations be administered in a transparent, nondiscriminatory and competitively neutral manner. Fourthly, the document includes commitments on the *licensing* process. If a license is required to provide telecommunications services, the criteria, terms and conditions of individuals licenses must be public. Reasons for denial of a license must be provided.

Finally, the signatories of the RP committed themselves to ensure *the independence and impartiality of the regulatory body*. Indeed, in many WTO countries where the provision of telephone service was the sole responsibility of the State, there was no separate body responsible for regulating prices or supervising practices. The United States' Federal Communications Commission (FCC) and the Canadian Radio-television and Telecommunications Commission (CRTC) were some of the rare independent regulators of telecommunications before the 1990s. With the coming of competition, the new entrants need to know that the rules of the game will be applied and enforced by an impartial referee and not an organization which is part of, or related to, the dominant telecommunications provider. Therefore, the RP stipulates that "the regulatory body is separate from, and not accountable to, any supplier of basic telecommunications services. The decisions of and the procedures used by regulators shall be impartial with respect to all market participants."

3. An evaluation of the Agreement on Basic Telecommunications

3.1. Significant commitments?

What is the significance of the Agreement on Basic Telecommunications and the Reference Paper? What did it really achieve? Skeptics would stress that most of the commitments taken as a result of the negotiations on basic telecommunications are *standstill commitments*, i.e. they consist in binding liberalizing measures that have already been adopted at the national or regional level (Noam, 1997).[4] This is especially true for industrialized countries. Canada, the United States, the

[4] Noam also points to the limits on foreign investment commitments that one finds in the Agreement on Basic Telecommunications and the delays on the implementation demanded by many developing countries as examples of the limitations of the ABT.

European Union and many others had already ended, or had taken formal engagements to end exclusive rights in telecommunications services and open the sector to domestic and/or foreign competition. Moreover, domestic regulations to support this move to greater competition were already adopted or under way. In fact, one can argue that WTO commitments in services, in general, are only binding liberalization initiatives which were already in place at the national or regional level. One could even point out that international agreements generally lag behind domestic policy.

However, if one adopts a more optimistic view of the ABT, one has to stress that a binding commitment to keep a sector open to foreign competition provides investors with the certainty and predictability that domestic liberalization alone cannot give. The "insurance policy" aspect of this agreement should not be neglected. Moreover, as the parties to the agreement took binding commitments regarding telecommunications services, the sector is now subject to a multilateral dispute settlement process, the WTO's Dispute Settlement Understanding (DSU). Furthermore, one could also note that the Agreement on Basic Telecommunications improved the situation which existed up to now in telecommunications services in many ways. Indeed, a detailed examination of the schedules of commitments points out a number of improvements. For example, even though the European Union had already planned to allow competition in telecommunications services on January 1st 1998, "EU members were under no obligation to extend market access privileges to non-EU members, nor were they subject to any penalty should they treat non-EU carriers in a discriminatory manner. Through the 1997 WTO commitments, the EU made a binding commitment to extend its current internal level of market access to non-EU service providers" (USITC, pp. 4–42). Similarly, Japan, Korea, Hong Kong and Singapore agreed to new liberalizations.

3.2. The Reference Paper on regulatory principles

Another important aspect of the agreement on telecommunications is that it took into account the importance of *domestic regulation* and of private actors' practices in its application of liberalization. The agreement acknowledges that liberalization requires more than "border measures", such as the reduction or elimination of tariffs. "Internal measures" are now considered potential barriers to trade and regulatory policies in particular have been subjected to greater scrutiny. Regulatory measures can impede market access in many ways, even if regulation is applied in a nondiscriminatory manner to domestic and foreign firms. The clearest examples of such barriers to entry are regulations which restrict the provision of a good or service to a single supplier. The granting of the monopoly does not violate GATS because Members may decide not to commit to market access in the sector or if they do, they may maintain clear quantitative restrictions on all or some sub-sectors. Moreover, commitments which formally allow very good access to a national market are not very valuable if the domestic dominant carrier engages in practices which prevent competitors from entering.

It is important to understand the nature of the regulatory principles put forward in that Reference Paper. The document does not oblige the signatories to adopt one single set of regulations regarding telecommunications services. Rather, it provides general principles to guide domestic policies. This is a strength, rather than a weakness, as some have suggested. In practice, the RP will make regulatory requirements and governmental policies of different jurisdictions more

similar and will result in a certain amount of policy convergence. Nevertheless, it remains that the objective is only to provide guidelines to respect. For example, national policymakers are free to adopt a variety of criteria in the granting of licenses, as long as they are public and transparent. Similarly, a country is free to establish a universal service system to ensure that everybody has access to the telecommunication network, as long as it is transparent and nondiscriminatory. The ABT is also agnostic regarding public ownership: in countries where the monopoly providers were state-owned, national policymakers do not have to privatize the incumbent to respect their commitments.

This approach to regulatory measures aim at striking a balance between two objectives: international market openness and national sovereignty. By trying to accommodate differences instead of attempting to harmonize them away, the trade rules for telecommunications services regulation respect the compromise at the heart of the trade regime, the compromise between trade liberalization and state sovereignty (Wolfe, 1999).

Despite the positive elements of the adoption of the Reference Paper on regulatory principles, one could argue that a *horizontal approach* to these questions would be a better strategy. In addition to a broader coverage, such an approach would allow a more coherent perspective on how competition policy and regulatory policy relate to trade policy. Nevertheless, the sectoral approach adopted for telecommunications presents some clear benefits. It allows Members to craft agreements which deal with the issues that are unique to that sector. For instance, in telecommunications services, specific anticompetitive practices have been targeted: cross-subsidization or retaining technical and commercial information which is necessary to the new entrant. The issue of interconnection was also directly dealt within a sectoral agreement, whereas a horizontal approach might not have succeeded in reaching an agreement on that level of details. The result is that Members know more precisely what they are committing to and it provides more specific language for a panel to base its analysis, if a Member resorts to the dispute settlement process. The sectoral approach may also be the only feasible one for the time being. To include competition policy and domestic regulation in the multilateral trade agreements can be seen as an important encroachment to national sovereignty by many WTO members.

One weakness that has been raised by lawyers about the regulatory principles in the ABT is that they lack precision. They argue that many of the concepts used in the text are vague. For example, the fact that the central notion of "major supplier" is defined in very general terms in the Reference Paper casts some doubts over the capacity of the document to create enforceable safeguards against anti-competitive behaviors (Bronkers & Larouche, 1997). Moreover, the Reference Paper identifies cross-subsidization as an anti-competitive practice. Bronkers and Larouche emphasize that it is difficult to monitor this cross-subsidization, as it demands the implementation of strict accounting, reporting, auditing and disclosure systems, which are not included in the RP. Other examples of the level of generality of the RP can be found in the section on universal service and in the provisions concerning licensing. Finally, one can ask if we need to specify benchmarks for elements like the delays for licensing decisions or interconnection fees or make the notion of "interconnection at any feasible point" clearer.

The question of the lack of precision can be considered from a legal perspective: it is difficult to enforce vague rules. On the other hand, one could praise the degree of regulatory flexibility granted by such broad definitions. Trade agreements have to accommodate differences in domestic regulation, in order to respect sovereign states' right to create national rules, while attempting to

limit the range of divergence, to limit the negative consequences for international trade. Moreover, it leaves scope for a much needed flexibility to experiment and identify the regulations which can best manage the transition from monopolized to competitive telecommunications markets. The future debates about modifying and strengthening the content of the Reference Paper on regulatory principles will have to take this tension into consideration.

4. Concluding remarks

In regard of future trade liberalization in telecommunications services, two main issues can be raised: the issue of domestic regulation and the issue of public ownership. The issue of government ownership strikes at the heart of the compromise between trade liberalization and state sovereignty. The members of the WTO are free to choose to privatize the public corporation which are providing telecommunications services or other types of services. There is no legal obligation on them to change the status of the operator, even if competition is introduced and committed on, except regarding the formal independence of the regulator.

However, there has been a shift from the view that telecommunication is a *public service* to be provided by the state, like other infrastructure services (electricity, transportation, post) to the view that these services are *commodities* like any other, can be traded between nations and be subjected to trade rules. This shift challenges the national public policies supporting state ownership of infrastructures. It is feared that the ownership link will grant a public corporation special privileges; for instance, the issue of the independence of the regulator vis-à-vis the state-owned incumbent was raised in this paper. The tension between the freedom of sovereign states to opt for a variety of policy instruments to achieve their goals and the existence of trade rules which somehow challenge the use of certain instruments such as public ownership is clear. However, the Agreement on Basic Telecommunications does not offer a comprehensive solution to this particular issue.

In contrast, regarding the issue of domestic regulation, the ABT appears to offer a model to deal with that tension. As discussed earlier, the Reference Paper on regulatory principles is an attempt to respect the regulatory autonomy of nation-states while making sure that domestic measures affecting the provision of telecommunications services do not impair trade. The provision on universal service is an especially clear example of efforts to strike this balance. The tension between sovereignty and the international trade system will remain and intensify in the next few years, as trade commitments will deepen, increasingly affecting national policies. One of the main challenges will be to find arrangements which will perpetuate the equilibrium, the compromise achieved up to now. The legitimacy of the trade system will be based on the respect of state sovereignty, especially in democratic nation-states where the expression of democratic will, and its concretisation through the actions of government, is seen as an important source of political legitimacy.

Adopting a broader economic perspective, one could finally argue that the ABT, as well as the Information Technology Agreement (ITA) concluded in 1997 which eliminates all tariffs on information technology equipment, are more important than trade agreements in other sectors, given the centrality of information and communications technologies for the current economic growth. Indeed, some economists analyzed the consecutive periods of economic growth and identified information technologies as the engine of the current "techno-economic paradigm"

(Freeman & Perez, 1988).[5] Indeed, according to their views, each growth period is fueled by a core technology which has great potential for multiple applications, innovations and increased productivity. The previous period (from the 1930s to 1980s) was based on cheap and abundant energy, especially oil. The new mode of growth is based on the multiple possibility of microchips. Allowing competition in the provision of telecommunications services could be seen as taking full advantage of the new technology-based growth as well as facilitating the diffusion of its benefits.

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[5] "Some changes in technology systems are so far-reaching in their effects that they have a major influence on the entire economy. A change of this kind carries with it many clusters of radical and incremental innovations, and may eventually embody a number of new technology systems. A vital characteristics of this type of technical change is that it has *pervasive* effects throughout the economy, i.e. it not only leads to the emergence of a new range of products, services, systems and industries in its own rights; it also affects directly or indirectly almost every other branch of the economy". (Freeman & Perez, 1988, p. 47).